[DISCUSSION DRAFT]

117TH CONGRESS
1ST SESSION

H. R. ______

To amend the Securities Exchange Act of 1934 to establish a Credit Rating Agency Assignment Board to assign qualified nationally recognized statistical rating organizations to issue credit ratings with respect to corporate issuers, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

M. ______ introduced the following bill; which was referred to the Committee on ______

A BILL

To amend the Securities Exchange Act of 1934 to establish a Credit Rating Agency Assignment Board to assign qualified nationally recognized statistical rating organizations to issue credit ratings with respect to corporate issuers, and for other purposes.

Be it enacted by the Senate and House of Representa-
tives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the “NRSRO Reform Act”.

1

2

3

4
SEC. 2. CREDIT RATING ASSIGNMENTS FOR CORPORATE ISSUERS.

(a) In General.—Section 15E of the Securities Exchange Act of 1934 (15 U.S.C. 78o–7) is amended by adding at the end the following:

“(w) CREDIT RATING ASSIGNMENTS FOR CORPORATE ISSUERS.—

“(1) Definitions.—In this subsection:

“(A) Board.—The term ‘Board’ means the Credit Rating Agency Board established under paragraph (2).

“(B) Qualified nationally recognized statistical rating organization.—The term ‘qualified nationally recognized statistical rating organization’ means a nationally recognized statistical rating organization that the Board determines, under paragraph (3)(B), to be qualified to issue credit ratings with respect to corporate issuers.

“(2) Credit rating agency board.—

“(A) In general.—Not later than 180 days after the date of enactment of this subsection, the Commission shall—

“(i) establish the Credit Rating Agency Board, which shall be a self-regulatory organization;
“(ii) subject to subparagraph (C), select the initial members of the Board; and

“(iii) establish a schedule to ensure that the Board begins assigning qualified nationally recognized statistical rating organizations to provide credit ratings not later than 1 year after the selection of the members of the Board.

“(B) Schedule.—The schedule established under subparagraph (A)(iii) shall prescribe when—

“(i) the Board will conduct a study of the securitization and ratings process and provide recommendations to the Commission;

“(ii) the Commission will issue rules and regulations under this section;

“(iii) the Board may issue rules under this subsection; and

“(iv) the Board will—

“(I) begin accepting applications to select qualified national recognized statistical rating organizations; and

“(II) begin assigning qualified national recognized statistical rating
organizations to provide credit ratings.

“(C) Membership.—

“(i) In general.—The Board shall initially be composed of an odd number of members selected from the industry, with the total numerical membership of the Board to be determined by the Commission.

“(ii) Specifications.—Of the members initially selected to serve on the Board—

“(I) not less than a majority of the members shall be representatives of the investor industry who do not represent issuers;

“(II) not less than 1 member should be a representative of the issuer industry;

“(III) not less than 1 member should be a representative of the credit rating agency industry; and

“(IV) not less than 1 member should be an independent member.
“(iii) TERMS.—Initial members shall be appointed by the Commission for a term of 4 years.

“(iv) NOMINATION AND ELECTION OF MEMBERS.—

“(I) IN GENERAL.—Prior to the expiration of the terms of office of the initial members, the Commission shall establish fair procedures for the nomination and election of future members of the Board.

“(II) MODIFICATIONS OF THE BOARD.—Prior to the expiration of the terms of office of the initial members, the Commission—

“(aa) may increase the size of the board to a larger odd number and adjust the length of future terms; and

“(bb) shall retain the composition of members described in clause (ii).

“(v) RESPONSIBILITIES OF MEMBERS.—Members shall perform, at a min-
imum, the duties described in this sub-
section.

“(vi) Rulemaking Authority.—The
Commission shall, if it determines nec-
essary and appropriate, issue further rules
and regulations on the composition of the
membership of the Board and the respon-
sibilities of the members.

“(D) Other Authorities of the
Board.—The Board shall have the authority to
levy fees from qualified nationally recognized
statistical rating organization applicants, and
periodically from qualified nationally recognized
statistical rating organizations as necessary to
fund expenses of the Board.

“(E) Regulation.—The Commission has
the authority to regulate the activities of the
Board, and issue any further regulations of the
Board it deems necessary, not in contravention
with the intent of this section.

“(3) Board Selection of Qualified Nation-
ally Recognized Statistical Rating Organiza-
tion.—

“(A) Application.—
“(i) IN GENERAL.—A nationally recognized statistical rating organization may submit an application to the Board, in such form and manner as the Board may require, to become a qualified nationally recognized statistical rating organization with respect to corporate issuers.

“(ii) CONTENTS.—An application submitted under clause (i) shall contain—

“(I) information regarding the institutional and technical capacity of the nationally recognized statistical rating organization to issue credit ratings;

“(II) information on whether the nationally recognized statistical rating organization has been exempted by the Commission from any requirements under any other provision of this section; and

“(III) any additional information the Board may require.

“(iii) REJECTION OF APPLICATIONS.—The Board may reject an application submitted under this paragraph if the nation-
ally recognized statistical rating organization has been exempted by the Commission from any requirements under any other provision of this section.

“(B) SELECTION.—The Board shall select qualified national recognized statistical rating organizations from among the nationally recognized statistical rating organizations that submit applications under subparagraph (A).

“(C) RETENTION OF STATUS AND OBLIGATIONS AFTER SELECTION.—An entity selected as a qualified nationally recognized statistical rating organization shall retain its status and obligations under the law as a nationally recognized statistical rating organization, and nothing in this subsection grants authority to the Commission or the Board to exempt qualified nationally recognized statistical rating organizations from obligations or requirements otherwise imposed by Federal law on nationally recognized statistical rating organizations.

“(4) REQUESTING A CREDIT RATING.—A corporate issuer which seeks a credit rating—
“(A) may not request a credit rating from a nationally recognized statistical rating organization; and

“(B) shall submit a request for a credit rating to the Board, in such form and manner as the Board may prescribe.

“(5) ASSIGNMENT OF RATING DUTIES.—

“(A) IN GENERAL.—For each request received by the Board under paragraph (4)(B), the Board shall select a qualified nationally recognized statistical rating organization to provide the credit rating to the corporate issuer.

“(B) METHOD OF SELECTION.—

“(i) IN GENERAL.—The Board shall—

“(I) evaluate the selection methods of either a lottery or blind rotating assignment system, incorporating the factors described in clause (ii), to reduce the conflicts of interest that exist under the issuer-pays model; and

“(II) prescribe and publish the selection method to be used under subparagraph (A).
“(ii) CONSIDERATION.—In evaluating a selection method described in clause (i)(I), the Board shall consider—

“(I) the information submitted by the qualified nationally recognized statistical rating organization under paragraph (3)(A)(ii) regarding the institutional and technical capacity of the qualified nationally recognized statistical rating organization to issue credit ratings;

“(II) evaluations conducted under paragraph (7);

“(III) formal feedback from institutional investors; and

“(IV) information from sub-clauses (I) and (II) to implement a mechanism which increases or decreases assignments based on past performance.

“(iii) PROHIBITION.—The Board, in choosing a selection method, may not use a method that would allow for the solicitation or consideration of the preferred na-
tional recognized statistical rating organizations of the corporate issuer.

“(iv) ADJUSTMENT OF PROCESS.—
The Board shall issue rules describing the process by which it can modify the assignment process described in clause (i).

“(C) RIGHT OF REFUSAL.—

“(i) REFUSAL.—A qualified nationally recognized statistical rating organization selected under subparagraph (A) may refuse to accept a selection for a particular request by—

“(I) notifying the Board of such refusal; and

“(II) submitting to the Board a written explanation of the refusal.

“(ii) SELECTION.—Upon receipt of a notification under clause (i), the Board shall make an additional selection under subparagraph (A).

“(iii) INSPECTION REPORTS.—The Board shall annually submit any explanations of refusals received under clause (i)(II) to the Commission, and such explanatory submissions shall be published in
the annual inspection reports required under subsection (p)(3)(C).

“(6) DISCLAIMER REQUIRED.—Each credit rating issued under this subsection shall include, in writing, the following disclaimer: ‘This credit rating has not been evaluated, approved, or certified by the Government of the United States or by a Federal agency.’.

“(7) EVALUATION OF PERFORMANCE.—

“(A) IN GENERAL.—The Board shall prescribe rules by which the Board will evaluate the performance of each qualified nationally recognized statistical rating organization, including rules that require, at a minimum, an annual evaluation of each qualified nationally recognized statistical rating organization.

“(B) CONSIDERATIONS.—The Board, in conducting an evaluation under subparagraph (A), shall consider—

“(i) the results of the annual examination conducted under subsection (p)(3);

“(ii) surveillance of credit ratings conducted by the qualified nationally recognized statistical rating organization after the credit ratings are issued, including—
“(I) how the rated instruments perform;

“(II) the accuracy of the ratings provided by the qualified nationally recognized statistical rating organization as compared to the other nationally recognized statistical rating organizations; and

“(III) the effectiveness of the methodologies used by the qualified nationally recognized statistical rating organization; and

“(iii) any additional factors the Board determines to be relevant.

“(C) REQUEST FOR REEVALUATION.—Subject to rules prescribed by the Board, and not less frequently than once a year, a qualified nationally recognized statistical rating organization may request that the Board conduct an evaluation under this paragraph.

“(D) DISCLOSURE.—The Board shall make the evaluations conducted under this paragraph available to Congress.

“(8) RATING FEES CHARGED TO ISSUERS.—
“(A) Limited to reasonable fees.—A qualified nationally recognized statistical rating organization shall charge a corporate issuer a reasonable fee, as determined by the Commission, for a credit rating provided under this section.

“(B) Fees.—Fees may be determined by the qualified national recognized statistical rating organizations unless the Board determines it is necessary to issue rules on fees.

“(C) Reasonable fee.—The Board shall issue regulations to define the term ‘reasonable fee’ for purposes of subparagraph (A).

“(9) Material change in circumstances.—If the Board determines that it is necessary or appropriate in the public interest or for the protection of investors, the Board may issue regulations requiring that a corporate issuer that has received a credit rating under this subsection request a revised credit rating each time the corporate issuer experiences a material change in circumstances, as defined by the Board.

“(10) Conflicts.—

“(A) Members or employees of the Board.—
“(i) Loan of money or securities prohibited.—

“(I) In general.—A member or employee of the Board shall not accept any loan of money or securities, or anything above nominal value, from any nationally recognized statistical rating organization, issuer, or investor.

“(II) Exception.—The prohibition in subclause (I) does not apply to a loan made in the context of disclosed, routine banking and brokerage agreements, or a loan that is clearly motivated by a personal or family relationship.

“(ii) Employment negotiations prohibition.—A member or employee of the Board shall not engage in employment negotiations with any nationally recognized statistical rating organization, issuer, or investor, unless the member or employee—

“(I) discloses the negotiations immediately upon initiation of the negotiations; and
“(II) recuses himself from all proceedings concerning the entity involved in the negotiations until termination of negotiations or until termination of his employment by the Board, if an offer of employment is accepted.

“(B) CREDIT ANALYSTS.—

“(i) IN GENERAL.—A credit analyst of a qualified nationally recognized statistical rating organization shall not accept any loan of money or securities, or anything above nominal value, from any issuer or investor.

“(ii) EXCEPTION.—The prohibition described in clause (i) does not apply to a loan made in the context of disclosed, routine banking and brokerage agreements, or a loan that is clearly motivated by a personal or family relationship.

“(11) EVALUATION OF CREDIT RATING AGENCY BOARD.—Not later than 5 years after the date that the Board begins assigning qualified nationally recognized statistical rating organizations to provide
credit ratings, the Commission shall submit to Con-
gress a report that provides recommendations of—

“(A) the continuation of the Board;

“(B) any modification to the procedures of
the Board; and

“(C) modifications to the provisions in this
subsection.”.

(b) Conforming Amendment.—Section
“subject to subsection (w) of section 15E,” before “cor-
porate”.